

The 2022-23 Budget: Overview of Proposition 98 Proposals



LEGISLATIVE ANALYST'S OFFICE

Update on the 2020-21 and 2021-22 Guarantees

(In Millions)

	2020-21			2021-22		
	June 2021 Estimate	January 2022 Estimate	Change	June 2021 Estimate	January 2022 Estimate	Change
General Fund	\$67,685	\$70,035	\$2,351	\$66,374	\$71,845	\$5,471
Local property tax	25,745	25,901	156	27,365	27,219	-146
Totals	\$93,430	\$95,936	\$2,507	\$93,739	\$99,064	\$5,325

Significant Increase in Current- and Prior-Year Estimates of the Guarantee

- Relative to the June 2021 estimates, the guarantee is up \$2.5 billion (2.7 percent) in 2020-21 and \$5.3 billion (5.7 percent) in 2021-22 (\$7.8 billion in total).
- These increases are due to higher General Fund revenue estimates. Many factors account for this increase—retail sales have surged, corporate earnings have reached historic highs, and employers’ payrolls have grown.
- The state is required to “settle up” to the higher guarantee. These one-time settle-up payments account for about one-third of the new Proposition 98 spending in the Governor’s budget.



Additional Growth in the Guarantee in 2022-23

(Dollars in Millions)

	2020-21 Revised	2021-22 Revised	2022-23 Proposed	Change From 2021-22	
				Amount	Percent
Funding by Source					
General Fund	\$70,035	\$71,845	\$73,134	\$1,289	1.8%
Local property tax	25,901	27,219	28,846	1,627	6.0
Totals	\$95,936	\$99,064	\$101,980	\$2,916	2.9%
Funding by Segment					
K-12 education	\$82,089	\$84,407	\$87,326	\$2,919	3.5%
Community colleges	10,766	11,075	11,593	518	4.7
Reserve deposit	3,081	3,582	3,061	-521	-14.5

Increase in the 2022-23 Guarantee

- The guarantee is up \$2.9 billion (2.9 percent) over the revised 2021-22 level and \$8.2 billion (8.8 percent) compared with the enacted 2021-22 level.
- Increases in General Fund and local property tax revenue both contribute to growth in the guarantee.

Adjustment for Transitional Kindergarten

- The June 2021 budget plan established a schedule to make Transitional Kindergarten available to all four-year olds by 2025-26. It also reflected an agreement to “rebench” (adjust) the guarantee upward to account for the cost of the expansion.
- The estimate of the guarantee in 2022-23 includes a General Fund increase of \$639 million for the first year of the Transitional Kindergarten expansion.



Proposition 98 Reserve Deposits and School District Reserves

Significant Deposits Into the Proposition 98 Reserve

- Proposition 2 (2014) established the Proposition 98 Reserve and set forth rules requiring deposits and withdrawals under certain conditions. Generally, deposits are required when revenue from capital gains is relatively strong and the minimum guarantee is growing faster than per capita personal income.
- The June 2021 budget plan assumed the state would make deposits totaling \$4.5 billion across 2020-21 and 2021-22. Under the Governor's budget, the state would make additional required deposits of nearly \$2.2 billion across those two years and another deposit of nearly \$3.1 billion in 2022-23.
- The total balance in the reserve would reach \$9.7 billion by the end of 2022-23—nearly 10 percent of the minimum guarantee.

School District Reserve Cap Operative in 2022-23

- A state law caps the reserves a school district may hold for undesignated purposes once the Proposition 98 Reserve exceeds 3 percent of the minimum guarantee.
- The cap is 10 percent of a school district's annual expenditures. Districts with 2,500 or fewer students are exempt.
- The latest available data (from 2019-20) show that approximately 265 medium and large districts (76 percent) have reserves exceeding the cap.
- Districts could avoid the cap by designating their reserves for specific purposes or asking their county offices of education to approve an exemption. Alternatively, they could spend down their reserves.



Comments on the Minimum Guarantee

Underlying Revenue Estimates Generally Seem Reasonable

- For 2021-22, the General Fund revenue estimate in the Governor’s budget is \$9.4 billion (4.7 percent) lower than our November estimate. Although the budget estimate is plausible, we think revenue is more likely than not to come in higher.
- For 2022-23, the General Fund revenue estimate in the Governor’s budget is \$9.9 billion (4.9 percent) lower than our November estimate. The majority of this difference is due to the Governor’s tax policy proposals. Accounting for these proposals, our estimates are similar.
- The estimates of local property tax revenue in the Governor’s budget also seem reasonable. (The budget estimates are only \$124 million above our estimates for 2021-22 and 2022-23 combined.)

Changes in General Fund Revenue Would Affect the Minimum Guarantee

- “Test 1” is operative for calculating the guarantee each year of the budget period. In Test 1 years, the guarantee increases or decreases about 40 cents for each dollar of higher or lower revenue.
- Attendance declines in 2021-22 or 2022-23 would not reduce the guarantee, even if they were significantly larger than the Governor’s budget assumes. The Test 1 formula ensures schools and community colleges receive at least 40 percent of General Fund revenue regardless of student attendance changes.



Overview of Proposition 98 Spending Proposals

Budget Contains \$17.7 Billion in Proposition 98 Spending Proposals

- Nearly \$10.6 billion for ongoing augmentations.
- Nearly \$7.2 billion for one-time activities.

\$5.3 Billion Ongoing to Fund Previous Budget Commitments

- The largest allocation is \$3.4 billion to accelerate implementation of the Expanded Learning Opportunities Program.
- Other allocations relate to Transitional Kindergarten, universal school meals, State Preschool rates, and community college financial aid.

\$4.1 Billion Ongoing for Cost-of-Living Adjustments (COLAs) and Attendance Changes

- The budget covers a 5.33 percent COLA for school and community college programs.
- For schools, the budget anticipates a 2.19 percent attendance decline in 2022-23 but proposes a new declining enrollment adjustment to offset this reduction.
- For community colleges, the budget funds 0.5 percent enrollment growth in 2022-23 and proposes a new funding floor for each college district beginning in 2025-26.

\$2.3 Billion One Time for Infrastructure

- For schools, the budget provides \$1.5 billion for electric school buses and \$450 million for kitchen infrastructure. (Separate from these amounts, the budget provides \$2.2 billion in non-Proposition 98 General Fund for the School Facility Program.)
- For community colleges, the budget provides \$388 million for deferred maintenance and instructional equipment.



K-12 Spending Proposals

(In Millions)	
Ongoing	
Expanded Learning Opportunities Program (ELOP)	\$3,400
LCFF attendance (-2.19 percent) and COLA (5.33 percent) adjustments	2,106
New LCFF adjustment for declining enrollment	1,200
Transitional Kindergarten expansion	639
Universal school meals implementation	596
Special Education base rates	500
Transitional Kindergarten lower staffing ratios	383
COLA for select categorical programs (5.33 percent)	352
State Preschool adjustment factor for students with disabilities	198
Annualization of State Preschool rate increases	166
After school program rates	149
Charter school facilities upgrades	30
California College Guidance Initiative	9
Personnel Management Assistance Teams (PMATs)	5
Agricultural vocational education	2
Subtotal	<u>(\$9,735)</u>
One Time	
Career pathways development	\$1,500
Green school bus grants	1,500
ELOP arts and music infrastructure	937
Literacy coaches and reading specialists	500
Inclusive Early Education Expansion Program	500
Dual enrollment access	500
School kitchen upgrades	450
Multilingual classroom libraries	200
Training on early identification of learning disabilities	60
Model curricula development	14
California College Guidance Initiative	4
School breakfast start-up grants	3
Subtotal	<u>(\$6,169)</u>
Total K-12 Education	\$15,904
LCFF = Local Control Funding Formula and COLA = cost of living adjustment.	



Community College Spending Proposals

(In Millions)	
Ongoing	
COLA for apportionments (5.33 percent)	\$409
Part-Time Faculty Health Insurance Program	200
Student Success Completion Grants (caseload adjustment)	100
COLA for select categorical programs (5.33 percent)	53
Technology security	25
Enrollment growth (0.5 percent)	25
Equal Employment Opportunity program	10
Financial aid administration	10
NextUp foster youth program	10
A2MEND program	1
Subtotal	<u>(\$843)</u>
One Time	
Facilities maintenance and instructional equipment	\$388
Student enrollment and retention strategies	150
Health care pathways for English learners	130
Common course numbering implementation	105
Technology security	75
Transfer reform implementation	65
Intersegmental curricular pathways software	25
STEM and health care pathways grant program	20
Emergency financial assistance for AB 540 students	20
Teacher credentialing partnership program	5
Umoja program study	— ^a
Subtotal	<u>(\$983)</u>
Total California Community Colleges	\$1,826

^a Reflects \$179,000.

COLA = cost of living adjustment; A2MEND = African American Male Education Network and Development; and STEM = science, technology, engineering, and mathematics.



Comments

Proposition 98 Budget Likely Prepared for Mild Recession

- The state could draw upon the \$9.7 billion in the Proposition 98 Reserve to maintain programs in the event of a downturn. (In some cases, the constitutional formulas would require withdrawals.)
- The Proposition 98 budget also contains a one-time cushion of more than \$4 billion (the amount of one-time proposals specifically attributable to 2022-23).
- If the guarantee were to decline, the reserve balance and the one-time cushion would provide a buffer, mitigating the likelihood of program cuts or payment deferrals.

Some Ongoing Proposals Seem Reasonable

- The major ongoing increases for schools relate to previous commitments or involve additional funding for existing programs. The proposals generally appear reasonable and align with previous cost estimates.
- Some community college proposals raise new issues and might be worth revisiting.

State Appropriations Limit Is a Key Budget Issue

- The state is \$2.6 billion above its limit across 2020-21 and 2021-22— even after accounting for proposed spending on infrastructure (which is exempt from the limit).
- The Legislature can respond to excess revenues by (1) lowering tax revenues, (2) spending more on exempt purposes (such as infrastructure or state emergencies), or (3) splitting the excess revenues between taxpayer refunds and one-time payments to schools and community colleges.
- If the Legislature were to shift funding from the Governor's infrastructure proposals to nonexempt priorities, the state would exceed the limit by a larger amount.



Recommendations

Fund Fewer New Initiatives Given Limited District Capacity

- Districts face many constraints on their capacity to implement new initiatives, including (1) cost pressures related to inflation and pensions, (2) disruptions and staffing challenges caused by the pandemic, and (3) uncertainty about future enrollment and program demand. Districts also are implementing many new initiatives funded in the June 2021 budget plan and developing plans for spending more than \$20 billion in one-time federal relief funding.
- We are concerned the Governor’s budget contains so many new initiatives that districts would be unable implement them all effectively.
- We recommend funding fewer new initiatives (in some cases, smaller amounts or longer periods for implementation could be reasonable compromises). This approach would avoid fragmenting efforts to improve services and outcomes for students.

Prioritize Proposals Addressing Clearly Defined Problems

- In deciding which initiatives to fund, we recommend using committee hearings to identify proposals that clearly address underlying problems and do not unnecessarily create new programs or initiatives.
- For example, the budget proposes \$1.5 billion to develop college and career pathways in certain fields. Given that the state already has several programs supporting college and career pathways, we recommend the Legislature not create a new program until it receives evidence that existing programs are insufficient and that the identified problem is best addressed with additional one-time funding.

